No. 20418

United States
COURT OF APPEALS
for the Ninth Circuit

CONTINENTAL CASUALTY COMPANY,
a corporation,

Appellant,

v..

JUSTIN N. REINHARDT, SEYMOUR L. COBLENS, NORMAN A. STOLL and MORTON A. WINKEL,

Appellees.

APPELLANT'S OPENING BRIEF

Appeal from the United States District Court for the District of Oregon

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STATEMENT OF JURISDICTION

This is an appeal from a final order of the United States District Court for the District of Oregon. It is an action by appellant for a declaratory judgment under the provisions of the Federal Declaratory Judgment Act, 28 U.S.C. Sec. 2201. Appellant issued a policy of professional liability insurance to appellees, attorneys at law practicing in Portland, Oregon. Appellees, having been

sued by a third party in the Circuit Court of the State of Oregon, demanded that appellant defend them. Appellant seeks a declaratory judgment that it is not obligated to defend the third party's state court action.

The appellant is a corporation organized and existing under and by virtue of the laws of the State of Illinois and is authorized to engage in the insurance business in the State of Oregon. It has no principal place of business within the State of Oregon. The appellees are individual attorneys, residents of the State of Oregon, members of the Oregon State Bar, and authorized to engage in the practice of law within the State of Oregon. The amount in controversy, exclusive of interest and costs, exceeds the sum of $10,000 and the Court below assumes jurisdiction by reason of diversity of citizenship and appellate jurisdiction is granted this court by Title 28, § 1291 U.S.C.A.

STATEMENT OF THE CASE

The case was tried before the District Court without a jury on the pretrial order. The trial was limited to the single issue of whether the plaintiff was obligated to defend any or all of the defendants in the action entited "*Fordham* v. *Reinhardt, et al*" in the Multnomah County State Court. The only evidence presented at the time of trial was the insurance policy issued by appellant to appellees, a copy of the complaint filed in the State Court against the appellees, a motion against the complaint filed by the appellees, and a copy of the order on

the hearing of the motion (Op. 3-4). The District Court opinion held that appellant was obligated to defend the appellees; this judgment is challenged by this appeal.

Appellant issued a lawyers' professional liability policy to appellees providing, *inter alia*:

> "To pay on behalf of the insured all sums which the insured shall become obligated to pay by reason of the liability imposed upon him by law for damages resulting from any claim made against the insured arising out of the performance of professional services for others in the insured's capacity as a lawyer or a notary public and caused by any act, error or omission of the insured or any other person for whose acts the insured is legally liable."

Exclusion (a) provides the policy is not applicable to:

> "* * * Any dishonest, fraudulent, criminal or malicious act or omission of the insured, any partner or employee; * * *."

Appellees Reinhardt, Coblens and Stoll are partners engaged in the practice of law in the State of Oregon. Subsequent to the issuance of appellant's policy, the defendant Mr. Morton Winkel (hereinafter referred to as "Winkel") was included as a named insured. Winkel and the defendant firm represented Mansfield & Company (hereinafter referred to as "Mansfield") a creditor of Metropolitan Materials Company (hereinafter referred to as "Metropolitan"). Since Metropolitan was insolvent, appellees were unable to collect a judgment against Metropolitan, due and owing to Mansfield.

Mr. Kalkhoven and Mr. Fordham were the princi-

pals of Metropolitan; Mr. Fordham was a certified public accountant. Winkel threatened to bring an action against Fordham and Kalkhoven individually upon the theory that they misrepresented the financial status of Metropolitan and, relying upon this representation, Mansfield was induced to extend credit to its detriment. Winkel further threatened to send a copy of the complaint to the State Board of Accountancy.

When Fordham refused to assume personal liability for Metropolitan's debt, Winkel made good his threat and filed an action on behalf of Mansfield against Fordham and Kalkhoven in Multnomah County Circuit Court. Three causes of action were stated. First, that financial statements made by Fordham in connection with the extension of credit to Metropolitan, and upon which Mansfield relied in selling insurance to Metropolitan, were false, were known to be false when prepared, and were presented to Mansfield to induce it to extend credit. Second, that Fordham was liable as a director of Metropolitan for operating with insufficient capital, which insufficiency jeopardized Metropolitan's contractual obligations to the prejudice of creditors. Third, that the transfers of certain Metropolitan assets by the principals, including Fordham, were intended to hinder, delay and defraud creditors of Metropolitan, including Mansfield. Making good the second portion of his threat, Winkel forwarded a copy of the complaint, with cover letter, to the State Board of Accountancy.

The Circuit Court of the State of Oregon held in favor of Fordham and his associates on the theory that

there was no intent to defraud and no reliance by Mansfield upon the representations (Op. 3).

Fordham then filed, in the Multnomah County Circuit Court, an action for trade libel against the appellees, alleging in part:

> "That the sending of a copy of the Summons and Complaint to the State Board of Accountancy and the publication of the Summons and Complaint thereby effected was a trade and professional libel; that said action was taken strictly as what is commonly termed 'blackmail' in an effort to induce payment by the plaintiff herein of sums which were not owed by him; that despite cautioning and requests by attorney John Faust, Jr. that said action not be taken, the same action was nevertheless taken with a malicious motive and solely for the purpose of attempting to blackmail the plaintiff herein and for the sake of humiliating and embarrassing the defendant [sic] before his professional licensing board within this state, there being no other possible motive for the publication of said Summons and Complaint to the said State Board of Accountancy and its presentation to the Executive Secretary and members of said Board."

Motions were interposed on behalf of the appellees, some of which were allowed. At the time of trial of the instant action, no amended complaint had been filed in conformance with the order of the circuit court.

Appellees contend that appellant, under its aforementioned policy, had a duty to defend the action instituted by Fordham. Appellant sought a declaratory judgment that no duty to defend existed. The district court decided

only this single issue; it held that the appellant was bound to defend the appellees on the theory that the allegations of the Fordham complaint were "sufficiently ambiguous to permit the advancement of many theories of liability" (Op. 4). Appellants bring this appeal.

SPECIFICATIONS OF ERROR

1. The district court erred in finding and concluding that the plaintiff was bound to defend the action filed against the defendants in the Circuit Court of the State of Oregon for the County of Multnomah by Leslie E. Fordham.

2. The district court erred in entering its order requiring plaintiff to defend the defendants in the state court action entitled "Leslie E. Fordham v. Reinhardt, et al" pending in Multnomah county, being Clerk's Registry No. 303-532.

3. The court erred in finding and concluding that the allegations of the Leslie E. Fordham complaint against the defendants were sufficiently ambiguous to present the advancement of many theories of liability and that the allegations of the complaint stated a cause of action within the coverage of the policy issued by the plaintiff to the defendants requiring the plaintiff to defend the action.

4. The court erred in failing to find and conclude the allegations of the Fordham complaint against the defendants clearly stated a cause of action within the policy coverage, and that plaintiff was not required to afford a defense to the defendants in the Fordham action.

5. Each of the above mentioned findings made and entered by the District Court are clearly erroneous.

6.. Each of the above mentioned conclusions of the district court are contrary to the evidence and the law.

SUMMARY OF ARGUMENTS

The duty to defend is measured by the face of the complaint filed against the insured. The Fordham complaint showed no claim stated potentially within the policy coverage; there was no ambiguity which would permit the inference of a claim covered by the policy. The Fordham complaint alleged conduct on the part of the assured which was excluded as "malicious." The Fordham complaint further alleged acts which did not constitute conduct within the assured's professional capacity as a lawyer.

ARGUMENT

1. The insurer's duty to defend is measured by the allegations of the complaint filed against the assured.

The duty to defend is not dependent upon the merits of the case, since an insurer is obligated to defend suits *within the policy coverage* even if the same are false, fraudulent or groundless. See *MacDonald* v. *United Pacific Insurance Co.*, 210 Or. 395, 399, 311 P.2d 425 (1957). The determination of the existence of a duty to defend must be made upon a comparison of the allegations of the complaint filed against the insured and the coverage of the policy issued to the insured. See *Isenhart* v. *Gen-*

eral Casualty Co., 233 Or. 49, 377 P.2d 26 (1962). A comparison of the pleadings in the case filed by Fordham against the appellees and the policy issued by appellant, particularly the provisions and exclusions quoted hereinbefore, make it clear that no duty to defend arose because the complaint presented a claim excluded by the policy. The policy covered activities of the insured while acting in his professional capacity of a lawyer or notary public; it specifically excluded malicious acts. The Fordham complaint alleged conduct not within the capacity as a lawyer and conduct which was malicious. Therefore, the complaint stated no claim potentially within the coverage of the policy.

The governing substantive of law is that of the state of Oregon. The Oregon court has recently affirmed its adherence to the general rule that an insurer's duty to defend is measured solely by the allegations of the complaint filed against its insured. In *Isenhart* v. *General Casualty Co.,* supra, 233 Or. 54, the Oregon Supreme Court stated:

* * * * *

> "There is some authority for the view that in determining whether it has a duty to defend the insurer must look beyond the allegations of the complaint filed against the insured and if the actual facts are such as to bring the case within the coverage of the policy, the insurer must accept the tender of defense. The contrary view has been adopted in this state. In accordance with the weight of authority, we have held that the obligation of the insurer to defend is to be determined by the allegations of the complaint filed against the insured.

> "We adhere to this view. The insurer contracts to indemnify the insured within certain limits stated in the policy. If the facts alleged in the complaint against the insured do not fall within the coverage of the policy, the insurer should not have the obligation to defend. If a contrary rule were adopted, requiring the insurer to take note of facts other than those alleged, the insurer frequently would be required to speculate upon whether the facts alleged could be proved. We do not think that this is a reasonable interpretation of the bargain to defend. It is more reasonable to assume that the parties bargained for the insurer's participation in the lawsuit only if the action brought by the third party, if successful, would impose liability upon the insurer to indemnify the insured."

For other decisions asserting the same rule, see *MacDonald* v. *United Pacific Insurance Co.,* supra; 50 A.L.R.2d, Annot.: "Allegations in third persons' action against insured as determining liability insurer's duty to defend" 458-512 (1956), relied upon by the Oregon Supreme Court in *MacDonald,* supra; *Blohm et al* v. *Glens Falls Insurance Co.,* 231 Or. 410, 417-418, 373 P.2d 412 (1962); *Jarvis et ux* v. *Indemnity Insurance Co.,* 227 Or. 508, 517, 363 P.2d 740 (1961). See also, *Journal Publishing Co.* v. *General Casualty Co.,* 210 F.2d 202, 208 (9th Cir. 1954) indicating that the duty to defend and the duty to indemnify are premised upon different considerations.

Oregon's adherence to the rule is clear. The reasons for the rule, some of which are asserted in the foregoing paragraphs from *Isenhart,* require no elaboration on the

part of appellant. The complaint filed by Fordham against the appellees fail to state a claim potentially within the coverage of the policy, and the appellant had no duty to defend.

2. The Fordham complaint alleged an excluded claim and appellant had no duty to defend.

The district court held that appellant had a duty to defend appellees in the Fordham action. The apparent basis of the Court's holding was that "the allegations in the circuit court complaint are sufficiently ambiguous to permit the advancement of many theories of liability" (Op. 4). Appellant asserts that this was clearly erroneous. A comparison of the Fordham complaint and the appellant's policy reveals that the claim is excluded. The conduct of Winkel was alleged to be malicious. The acts of Winkel did not constitute conduct of a lawyer in his professional capacity. The theory of recovery was clearly delineated in the Fordham complaint; it was not ambiguous and no theory of recovery alleged would bring the claim within the potential policy coverage.

The insurer's duty to defend is limited to those causes potentially within the policy coverage. If a cause is stated potentially within the policy coverage, then the insurer is obligated to defend, regardless of whether the claim is false, fraudulent or groundless. The converse is also true; a valid claim need not be defended if, on the face of the complaint, no claim within the policy coverage is stated. The duties of defense and indemnity are distinct.

(A) *The appellees conduct was malicious, and was excluded from coverage by the policy.*

The district court's ruling that appellant had a duty to defend appellees was clearly erroneous since the Fordham complaint alleged conduct which was "malicious" and hence excluded under exclusion (a).

Appellant has been unable to discover a factually apposite case involving a lawyer's professional liability policy. The Fordham complaint alleged a cause of action for trade libel; paragraph XIV alleged that the sending of the complaint to the State Board of Accountancy was done for the purpose of "blackmail" and with a "malicious motive." Exclusion (a) provided that the policy was inapplicable to "any dishonest, fraudulent, criminal or malicious act." On this comparison of the complaint and the policy, then, no claim was stated potentially within the policy coverage.

Appellees contended in the district court that this exclusion applied only to "actual malice" existing in the mind of the insured and then only excluded indemnity; further, it was contended that "malice" was an ambiguous term, having at least two meanings in defamation cases.

First, there is nothing in law or fact to warrant the assertion that the "malice" exclusion applies only to the duty to indemnify.

Second, "malice" in common parlance means ill will against a person, but legally the Oregon Supreme Court has said it means wrongful acts intentionally done with-

out just cause or excuse. *Jaco* v. *Baker,* 174 Or. 191, 148 P.2d 938 (1944). "Malicious" means to harbor malice, ill will or enmity, or to have a bent to do evil or a deliberate intent to injure another. *Cook* v. *Kinzua Pine Mills Co., Inc.,* 207 Or. 34, 293 P.2d 717 (1956).

Third, since malicious acts are excluded, the appellant is not bound to search behind the face of the Fordham complaint in order to determine what meaning or meanings were attached to the word "malicious." Malicious acts are excluded from coverage; the complaint alleges a malicious tort; therefore, there is no duty to defend. If appellant were required to investigate the meaning attached to verbiage in the complaint, the force of the *Isenhart* rule, supra, would be destroyed or circumvented.

A somewhat analogous case involving a druggist's liability policy is *Hewit Pharmacy* v. *Aetna Life Insurance Co.,* 267 N.Y. 31, 195 N.E. 673 (1935). The policy provided for indemnity for damages resulting from death or bodily injury accidentally suffered in consequence of any "error or mistake" during the policy period arising out of "preparing, compounding, dispensing, selling or delivering at or from the premises" any "drugs, medicines or merchandise customarily kept for sale in drug stores." There was a policy exclusion for injuries or death caused by employees in violation of law or caused by failure to comply with any statute or local ordinance or in consequence of any unlawful act.

The insured operated both at retail and wholesale. One of its clerks, by mistake and without any intent to

violate the law, failed to label a certain drug which she believed was being sold at wholesale (where labelling was not required) when in fact it was being sold at retail (where labelling was required). As a result, the purchaser's wife drank the poison and died. The court held that the selling of the product without the label was an unlawful act committed by an employee of the insured and, therefore, came directly within the exclusion.

The cases would indicate that a communication of the complaint to the State Board of Accountancy might be subject to a qualified privilege, whether done by Winkel in his individual capacity or his capacity as a lawyer. However, the conduct is still actionable, despite the qualified privilege, if the act were maliciously done. Therefore, since the policy excludes malicious acts, and since the only unprivileged basis for the claim would be a malicious act, the conduct was excluded and appellants had no duty to defend.

Appellants respectfully submit that the act charged was malicious, that the policy excluded malicious acts, and therefore the appellant had no duty to defend.

(B) *The conduct of Winkel was not an "act arising out of the performance of professional services for others in the assured's capacity as a lawyer."*

The foregoing effectively shows that the ruling of the district court was clearly erroneous. The court reserved consideration of evidence and ruling upon appellants' further contention that the appellees' acts did not constitute conduct as a lawyer. However, appellant con-

tends that on the face of the complaint it is apparent that Mr. Winkel was not acting in his capacity as a lawyer at the time of the alleged tort.

Lawyers' professional liability policies seldom have been discussed by the courts. The few decisions rendered do not seem apposite to the issues raised herein. See generally, 72 A.L.R.2d Annot., "Coverage, and exclusions, of liability or indemnity policy on attorney at law," 1249-1251 (1960).

American Fire and Casualty Co. v. *Kaplan,* 183 A.2d 914 (Mun. Ct. D.C. 1962) involved a negligent doing of an act which was clearly within one's professional capacity as a lawyer. *Strauss* v. *New Amsterdam Casualty Co.,* 216 N.Y. Supp. 2d 861, 30 Misc. 2d 345 (1961) involved a policy worded differently from that issued by appellant; the New York court held that an action for money had and received was not encompassed by a "malpractice, error or mistake" policy. *Cadwallader* v. *New Amsterdam Casualty Co.,* 396 Penn. 582, 152 A.2d 484 (1959) involved a negligent act, error or omission which was clearly conduct within the assured's capacity as a lawyer.

Lacking controlling authority, the issue must be determined by an examination of the policy language, the conduct of Winkel, basic legal principles, and pertinent analogies.

The policy provided coverage for claims:

> "* * * made against the insured arising out of the performance of professional services for others

> in the insured's capacity as a lawyer * * * caused by any act, error or omission of the insured * * *."

The obvious purpose of the clause is to limit the insurer's liability to conduct of the insured as a lawyer. The insurer is entitled to limit its obligations by appropriate language and the court will not rewrite the policy where this has clearly been done.

Appellant contends that the conduct of Winkel charged in the Fordham complaint was not action as a lawyer. The complaint charges Winkel with a trade or professional libel by means of a specific act: mailing a copy of the complaint to the State Board of Accountancy. The filing of a complaint on behalf of a client is not the challenged act.

While pleadings filed in an action or suit are public records, the transmission of a copy of a filed pleading, with or without comment, may constitute defamation; that is precisely the only theory possible on the face of the Fordham complaint. Several cases involving professional liability policies have considered analogous issues.

In *Kime* v. *Aetna Casualty & Surety Co.*, 66 Ohio App. 277, 33 N.E.2d 1008 (1940), it was held that an indemnity policy insuring an optometrist against damages resulting from loss or expense on account of malpractice, error or mistake in the practice of optometry did not cover the malpractice of an optometrist in doing things not covered by the statutory definition of optometry. Thus, the removal by the optometrist of certain particles from a patient's eyes by objective means was not the practice of

optometry as defined by the statute and the insurance company was not liable under its policy for injury to the patient's sight.

In *Crenshaw* v. *United States Fidelity & Guaranty Co.,* 193 S.W.2d 343 (Mo. 1946), the defendant insured the plaintiff "for professional services rendered * * * and resulting from any claim or suit based upon malpractice, error, negligence or mistake, breach of implied contract, loss of service, property damage, autopsies, inquests, personal restraints, the dispensing of drugs or medicine, assault, slander, libel * * *."

The decedent's wife filed an action against the insured for an unlawful autopsy performed upon the body of her husband. The basis of the cause of action was that the insured, as county coroner, permitted local university medical students to perform the autopsy. The insurer refused to defend, and when a judgment was had against the insured, the judgment creditor guarnisheed the insurance company. The court held that the insurance company had no coverage because its liability was restricted to acts performed in the insured's professional capacity as a physician and surgeon, and did not extend to acts performed in his official capacity as coroner.

In *Glesby* v. *Hartford Accident & Indemnity Co.,* 6 Cal. App 2d 89, 44 P.2d 365 (1935) an injury occurred to a patient resulting from treatment by an osteopathic physician's unlicensed assistant knowingly permitted by the physician. The California court held that the claim was not covered by the liability policy issued to the physician which excluded injuries caused while engaged in performing an unlawful act.

In order to justify the challenged conduct, appellees must indicate that, in some manner, the gratuitous mailing of the complaint to the State Board of Accountancy was the performance of a professional service. Appellant is unable to apprehend how this could be. How would the forwarding of a complaint to the State Board of Accountancy aid in the collection of a debt for appellee's client within the scope of conduct authorized by the canons of professional ethics? If a formal complaint were to be made to the professional board, regarding the conduct of Mr. Fordham, should not this complaint be made by the party injured (and presumably in possession of the facts) and not his attorney? If a complaint were to be made, why wasn't it done by normal channels, instead of mailing a copy of a pleading?

(C) *The Fordham complaint was not "sufficiently ambiguous as to allow recovery on many theories of liability."*

What the district court apparently held was that the Fordham complaint was sufficient to support several theories of recovery, some of which would be covered by appellant's policy. With this statement, appellants disagree.

The complaint sounded in trade libel; it was so labeled and pleaded. Appellant is unable to conjure up any theory of recovery not excluded by the policy. The complaint was hardly ambiguous. It set forth facts substantially as outlined in this brief, supra. Since the district court did not favor the parties with examples to support its statement, appellant can only conclude that it had no examples and appellant is unable to provide any.

CONCLUSION

The district court ruling that appellant had a duty to defend appellees in the Fordham action was clearly erroneous and should be reversed. The Fordham complaint alleged a malicious tort and exclusion (a) excluded malicious acts from coverage. Moreover, the Fordham complaint disclosed conduct on the part of the insured which was not conduct as a lawyer performing professional services. The ruling of the district court has no basis in law or fact.

Respectfully submitted,

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CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

KENNETH E. ROBERTS
Of Attorneys for Appellants